85-550

Supreme Court, U.S.
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No. 85-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

UNION OIL COMPANY OF CALIFORNIA,
Petitioner,

v.

SARAH M. SPAETH,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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September 30, 1985

QUESTION PRESENTED

Whether a party may be penalized through an award of punitive damages in a tort action for participating in a state administrative proceeding, where such participation is not shown to be engaged in for some purpose other than prevailing on the merits.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

No. 85——

UNION OIL COMPANY OF CALIFORNIA,
Petitioner,

v.

SARAH M. SPAETH,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

Union Oil Company of California ("Union") petitions for a writ of certiorari to review a judgment of the United States Court of Appeals for the Tenth Circuit.[1]

OPINIONS BELOW

The opinions of the court of appeals (App. A and App. B) are reported at 762 F.2d 865 and 710 F.2d 1455, respectively; the orders and opinions of the district court (App. C and App. D) are unreported.

JURISDICTION

The judgment of the court of appeals was entered May 24, 1985. Petitioner timely requested rehearing and sug-

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[1] The parties below were plaintiff Sarah M. Spaeth and defendant Union. Union is a wholly-owned subsidiary of Unocal Corp. The only affiliate of Union not wholly owned either by Union or by Unocal Corp. is Magma Power Co., a Nevada corporation.

gested rehearing *en banc* to the court of appeals, which denied both in an order dated July 2, 1985 (App. E), making the petition for certiorari due on September 30, 1985. This Court has jurisdiction to issue the requested writ under 28 U.S.C. § 1254(1) (1983).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The First Amendment to the United States Constitution provides:

> "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the Government for a redress of grievances."

The Fourteenth Amendment to the United States Constitution provides in relevant part:

> "No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law. . . ."

Oklahoma Statutes Annotated, Title 23 § 9 (1955) provides:

> "In any action for the breach of an obligation not arising from contract, where the defendant has been guilty of oppression, fraud or malice, actual or presumed, the jury in addition to the actual damages, may give damages for the sake of example, and by way of punishing the defendant."

STATEMENT

Introduction

Respondent Sarah M. Spaeth owns one-half of the mineral rights in a tract of land in Blaine County, Oklahoma. In 1956, respondent's predecessor in interest executed a

lease giving Union the right to explore for oil and gas on the property and to produce such oil and gas as it found. After initial exploration revealed significant gas reserves in the area of respondent's property, Union in 1965 sought and obtained a spacing order authorizing it to drill a series of wells, including a single well on respondent's property. Under Oklahoma state law, no operator may drill more than one well per spacing unit without authorization from the state Corporation Commission.[2]

Pursuant to the spacing order, Union drilled a well on respondent's property which, since 1967, has produced gas in paying quantities, resulting in royalties for respondent and other owners of the mineral rights in the land. In 1976, however, respondent decided that she would benefit if Union were to drill a second well on her property. Accordingly, on January 29, 1976, respondent petitioned the Corporation Commission requesting that the spacing order be modified to permit the drilling of a second well on her land.[3] Thereafter, on October 25, 1976, respondent wrote to petitioner Union requesting that a second well be drilled. Union responded negatively to respondent's request, in part because the low price of gas would not justify the cost of drilling a second well and in part because the outstanding spacing order of the Corporation Commission (then being challenged by respondent) would not permit it.

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[2] Okla. Stat. Ann., Title 52 § 87.1(a) (1969).

[3] This was not the first time that such a request had been made with respect to respondent's property. In 1975 a third party working with respondent made a similar petition to the Commission. That application was withdrawn after the Commission's trial examiner recommended after a hearing that the application be denied. Report of the Commission to Permit Additional Well to Be Drilled Within Established Morrow Spacing Unit, Cause CD No. 40701, Order No. 113411 (Corp. Comm'n Okla. June 12, 1975).

At the hearing on respondent's application on May 7, 1976, Union and other lessees in the area appeared in opposition, arguing that respondent had put forward no new evidence that would justify revision of the Commission's 1965 order. On June 22, 1976, the Commission issued its Findings and Order agreeing with Union and denying the application. App. F.

Respondent appealed the June 1976 order of the Commission to the Oklahoma Supreme Court. Once again Union appeared through counsel, arguing that the Commission had correctly concluded that respondent failed to make an adequate factual showing that the 1965 spacing order should be revised. On May 8, 1979, the Oklahoma Supreme Court reversed the Corporation Commission, finding that respondent, as the only party presenting evidence at the June 22, 1976 hearing, had carried her burden of showing that circumstances had changed sufficiently to justify increasing the number of authorized wells on respondent's property to two. App. G. After Union had unsuccessfully sought to reopen the proceedings on remand to the Commission for the taking of additional evidence, the Corporation Commission issued the new order on December 20, 1979. Union, having meanwhile negotiated a higher price from its gas purchaser, promptly offered to drill a second well. Respondent declined this offer, however, preferring to pursue her legal and equitable remedies as described below.

Proceedings Below

Shortly before the Oklahoma Supreme Court issued its decision overruling the Corporation Commission, respondent had begun an action in Oklahoma state court against Union seeking actual and punitive damages, as well as cancellation of her lease with Union, for what she claimed was Union's breach of an implied covenant to protect her land from drainage by drilling an additional well. This action was subsequently removed to federal district court because of diversity of citizenship.

At the trial in 1981 respondent sought some $25 million in punitive damages under the Oklahoma statute providing for punitive damages in non-contract cases where there is shown to have been "oppression, fraud or malice, actual or presumed." [4] In making the claim for punitive damages, counsel for respondent relied on Union's opposition before the Commission and the Oklahoma Supreme Court and specifically characterized as "malicious" Union's request for a further hearing before the Commission after the case had been remanded by the Supreme Court.[5] Over Union's objections, the trial court allowed the jury to consider respondent's claim for punitive damages even though no evidence had been submitted to show that Union's position before the Commission and the Oklahoma Supreme Court had no basis in fact or was taken for the purpose of harassing respondent.

After very brief deliberation, the jury returned a verdict for respondent awarding $22,807.00 in actual damages and $3 million in punitive damages. Less than a week thereafter, the court ordered Union's lease with respondent cancelled except as to the portion that had been developed through the drilling of the single well originally authorized by the Corporation Commission. Union immediately moved for a judgment notwithstanding the verdict asserting, among other things, that the issue of punitive damages should not have been submitted to the jury because Union "may not now be penalized for its efforts to lawfully pursue its legal remedies before the Corporation Commission." [6] The district court denied Union's motion.

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[4] Okla. Stat. Ann., Title 23 § 9 (1955).

[5] Transcript of Proceedings held on March 9 through March 11, 1981 at 543-44, *Spaeth v. Union Oil Co.*, No. C-79-345-T (W.D. Okla. Mar. 11, 1981).

[6] Brief of Union Oil Company of California in Support of Motion for Judgment N.O.V., or in the Alternative, a New Trial at 13, *Spaeth v. Union Oil Co.*, No. Civ. 79-345-T (W.D. Okla. Apr. 2, 1981).

On appeal to the Court of Appeals for the Tenth Circuit, Union argued once again that the only basis for the award of punitive damages was Union's participation in the Corporation Commission proceedings and the subsequent appeal and that such an exercise of constitutional rights "simply cannot be the basis of punitive damages" consistent with due process.[7] Although Union did not expressly refer to the First Amendment in presenting its appeal to the court of appeals, Union's invocation of the due process clause necessarily implicated the panoply of First Amendment rights subsumed under the due process clause of the Fourteenth Amendment and made applicable to the States thereby.[8] The court of appeals affirmed the trial court's judgment as to Union's liability, but remanded the case for a reduction of the actual and punitive damage awards. App. B. In its opinion the court of appeals did not address Union's argument that the award of any punitive damages in this case was in violation of Union's constitutional right to appear before the Corporation Commission and the Oklahoma Supreme Court.

On remittitur, the actual damage award was reduced to $17,542 and the plaintiff remitted $1 million of the $3

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[7] Brief of Appellant at 23, *Spaeth v. Union Oil Co.*, No. 81-1752 (10th Cir. Nov. 19, 1981); *see also id.*, at 10-11, 23-26; Reply Brief of Appellant at 18, *Spaeth v. Union Oil Co.*, No. 81-1752 (10th Cir. Feb. 16, 1982) ("To allow punitive damages to be assessed against UNION for UNION's pursuit of its legal remedies would be to deprive UNION, not only of the remedies themselves, but of the due process of law afforded by the Constitutions of the State of Oklahoma and the United States. UNION cannot be held liable for lawfully pursuing its legal remedies" (citations omitted)).

[8] *See* n. 12, p. 8, *infra*. Union's other arguments on appeal concerned Oklahoma state law concerning the covenant to prevent drainage, the role of the Corporation Commission in authorizing the drilling of new wells, the scope of the Oklahoma punitive damages statute, the propriety of the jury instructions, the lack of any pecuniary loss by respondent, and the excessiveness of the punitive damages awarded. Although Union believes that the court of appeals was in error on each of these issues (save the last), it does not seek this Court's review on any of these matters.

million in punitive damages. App. C. Union once again appealed to the Tenth Circuit, this time on the issue of punitive damages alone. On this second appeal, Union once again asserted that the award of punitive damages against Union for the exercise of its constitutional right to appear before the Corporation Commission was improper.[9] Once again the court of appeals issued an opinion, this time affirming the punitive damages award, without even discussing Union's constitutional argument.[10]

Union's petition for rehearing and suggestion for rehearing *en banc* were denied by the court of appeals on July 2, 1985, without opinion. App. E.

REASONS FOR GRANTING THE WRIT

The right given by the First Amendment to petition state and federal government officials is an important part of our heritage. Apart from the limited area of defamation, however, this Court has yet to decide the extent to which the constitutional right of petition limits the applicability of state tort law. Furthermore, the number of decisions of lower federal and state courts reconciling such tort law with the right to petition indicates the frequency with which this issue arises. Although generally the courts have upheld the constitutional right and refused to apply the state tort law, the result in this case shows that this is not always the case. The failure of the court below to recognize the right-

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[9] Brief of Appellant at 16, *Spaeth v. Union Oil Co.*, No. 84-1766 (10th Cir. Aug. 14, 1984) ("UNION is . . . being punished for its exercise of its right to due process—the right to appear before the Corporation Commission and express its position regarding the prevention of waste and the protection of correlative rights").

[10] App. A. The court of appeals did, however, make clear that the fact of Union's participation in the Commission proceedings was a substantial factor in the award of punitive damages. *Id.* at 4a ("The defendant's conduct in maliciously allowing drainage of plaintiff's gas and in opposing her attempts to obtain relief [from the Commission] . . . must be considered" in upholding the punitive damage award of $2 million.)

of-petition issue and to apply the teachings of this Court regarding that right warrant review. Certiorari should be granted to establish the constitutional limits on the extent to which state tort law can be used to punish persons for their participation in judicial or administrative proceedings.

The First Amendment to the United States Constitution by its terms guarantees "the right of the people . . . to petition the government for a redress of grievances." As this Court recently has observed, "the values in the right of petition as an important aspect of self-government are beyond question." [11] The right is therefore applicable to the states by incorporation through the Fourteenth Amendment's guarantee of due process.[12] And it extends to corporations, as well as to individuals.[13]

There are a number of circumstances in which state law can impinge upon the activities of an individual or corporation in petitioning the government. The issue can arise, for example, when one party sues another under state law of malicious prosecution for the defendant's suing the plaintiff.[14] It has arisen in a variety of cases

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[11] *McDonald v. Smith*, 105 S. Ct. 2787, 2790 (1985).

[12] *See DeJonge v. Oregon*, 299 U.S. 353 (1937); *Hague v. Committee for Indus. Org.*, 307 U.S. 496 (1939). In addition, the guarantee to each citizen of the "privileges and immunities" associated with United States citizenship has been construed since the earliest days of the Fourteenth Amendment to bar any state from interfering with a person's right to petition for redress of grievances. *See Twining v. New Jersey*, 211 U.S. 78 (1908); *United States v. Cruikshank*, 92 U.S. 542 (1875).

[13] *First Nat'l Bank v. Bellotti*, 435 U.S. 765, 778-86 (1978).

[14] *See City of Long Beach v. Bozek*, 183 Cal. Rptr. 86, 645 P.2d 137 (1982) (action for malicious prosecution arising from defendant's unsuccessful suit against city and two officers for false imprisonment); *Cate v. Oldham*, 707 F.2d 1176 (11th Cir. 1983) (injunction against malicious prosecution action brought by state attorney unsuccessfully sued for negligence in failing to protect deceased wife from her husband); *Grip-Pak, Inc. v. Illinois Tool Works, Inc.*, 694 F.2d 466, 471 (7th Cir. 1982) (malicious prosecution action

where the gravamen of the charge under state law has been tortious interference with some business relationship.[15] Parties have invoked the First Amendment protection of their right to petition when faced with proceedings under state unfair competition laws.[16] And, as in the present case, the issue can arise when one party seeks punitive damages under state tort law based upon the "aggravating circumstance" of the defendant's exercise of its right to petition for redress to state or federal authorities.[17]

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arising from defendant's unsuccessful prosecution of suit for theft of trade secrets); *Matossian v. Fahmie*, 101 Cal. App. 3d 128, 161 Cal. Rptr. 532 (1980) (malicious prosecution action brought by liquor licensee against other licensee for trying to influence public officials not to renew plaintiff's license).

[15] *See, e.g., Gorman Towers, Inc. v. Bogoslavsky*, 626 F.2d 607, 615 (8th Cir. 1980) (defendants petitioned the city's board of directors to rezone a particular site to prevent plaintiffs from constructing a highrise apartment complex on that site); *Sierra Club v. Butz*, 349 F. Supp. 934, 938 (N.D. Cal. 1972) (defendants sought to persuade the government to abandon its intention to permit logging in a particular wilderness area despite a contract allowing plaintiff to harvest in that area); *Mayer v. Wedgewood Neighborhood Coalition*, 707 F.2d 1020 (9th Cir. 1983) (defendants opposed construction of rental housing by plaintiff in several administrative proceedings); *Aknin v. Phillips*, 404 F. Supp. 1150 (S.D.N.Y. 1975) (defendants allegedly conspired to close down plaintiff's discotheque); *Sawmill Products, Inc. v. Town of Cicero*, 477 F. Supp. 636 (N.D. Ill. 1979) (defendants tried to prevent licensing of plaintiff's sawmill); *Arlington Heights Nat'l Bank v. Arlington Heights Federal Savings and Loan Ass'n*, 37 Ill. 2d 546, 229 N.E. 2d 514 (1967) (defendants allegedly induced village to breach its contract with plaintiff for vacation of a street); *First Nat'l Bank v. Marquette Nat'l Bank*, 482 F. Supp. 514 (D. Minn. 1979) (defendant lobbied for the passage of the Minnesota Bank Credit Card Act which caused damage to plaintiff).

[16] *Suburban Restoration Co. v. ACMAT Corp.*, 700 F.2d 98 (2d Cir. 1983).

[17] *See, e.g., Grybauskas v. Associated Estates Corp.*, 367 N.E.2d 881 (Ohio Ct. App. 1976) (punitive damages awarded for, among other things, filing of legal action simply for purpose of "annoying and harassing").

Despite the number and variety of circumstances in which First Amendment rights may come into conflict with state law, this Court has addressed the question thus far principally with respect to state law of defamation. Most often, of course, it has been the right of freedom of speech and press that has come into conflict with state dafamation laws.[18] But last term in *McDonald v. Smith*, the Court dealt with a case in which the allegation was that it violated a party's right to petition under the First Amendment to hold him liable for making factual representations to the President of the United States. The particular question presented for the Court's decision was not whether the First Amendment protection of the right to petition limited the scope of state defamation law. The Court assumed that it did, invoking, among other things, its prior, related decisions with respect to defamation under the First Amendment protection of speech and press. Rather, the question for the Court in *McDonald v. Smith* was whether state law could punish a petitioner for defamation in connection with a petition to the President even if the petition contained factual assertions that the petitioner knew to be false. The Court ruled that, rather than an absolute privilege, the right to petition (like the protection for freedom of speech and press) protected only statements not knowingly or recklessly false.

Given the Court's concentration on the area of defamation, it should not be surprising that state and lower federal courts sometimes fail to appreciate the constitutional limitations that the right to petition places on state law in other areas, such as malicious prosecution or the award of punitive damages.[19] Indeed, the very con-

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[18] *See, e.g., Gertz v. Robert Welch, Inc.*, 418 U.S. 323 (1974); *Rosenbloom v. Metromedia, Inc.*, 403 U.S. 29 (1971); *New York Times Co. v. Sullivan*, 376 U.S. 254 (1964).

[19] In *Gertz*, of course, the Court considered the question of punitive damages in the libel context and concluded that "actual malice" in the sense of knowledge of falsity or reckless disregard of truth

stitutional standards articulated by the Court with respect to state law of defamation make it unlikely that lower courts will apply these decisions in other contexts. Asking whether a speaker has shown a reckless disregard for the truth of his statements, while perfectly sensible when the question is one of whether the right of free speech has been abused, will often have little or no value when the question is abuse of the right of petition. Thus, in the present case respondent has not suggested that Union said anything false to the Corporation Commission or the Oklahoma Supreme Court; respondent's claimed grievance, rather, is that Union participated in the proceedings at all.

To find the relevant analytical framework for determining what respondent would have to prove to have Union penalized for exercising its right to petition, one must leave this Court's First Amendment decisions concerning state defamation law and turn to decisions interpreting federal statutes in the light of the right to petition. Thus, under the Sherman Act the Court has developed the doctrine that a defendant can be held liable only with respect to participation in judicial, administrative, or legislative proceedings that constitutes a mere "sham." [20] Similarly, the Court recently ruled that the National Labor Relations Board could not order an employer to cease

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or falsity was required where the speech involved issues of public concern. *Gertz v. Robert Welch, Inc., supra,* 418 U.S. at 347. Last Term the Court ruled that actual malice would not be required for punitive damages in a libel case involving neither a public figure nor speech concerning issues of public concern, with three Justices joining a plurality opinion saying less constitutional protection should be given to such speech and two Justices joining in the judgment because of their view that *Gertz* should be overruled. *Dun & Bradstreet, Inc. v. Greenmoss Builders, Inc.,* 105 S.Ct. 2939 (1985).

[20] *See California Motor Transport Co. v. Trucking Unlimited,* 404 U.S. 508 (1972); *United Mine Workers v. Pennington,* 381 U.S. 657 (1965); *Eastern R. R. Presidents Conference v. Noerr Motor Freight, Inc.,* 365 U.S. 127 (1961).

its legal action pending in state court absent a showing that the action is not "well founded." [21] Although these decisions technically have been based upon an interpretation of the federal statute involved, each has expressly resulted from the Court's concern for the First Amendment protection of the right to petition.

Perhaps because of the different context in which the question was raised, the court of appeals utterly failed here to appreciate or deal with the need to reconcile Union's constitutional right to petition with respondent's reliance on Union's exercise of that right to establish malice justifying the award of punitive damages. Thus, the court below did not consider whether Union's opposition to respondent's request for administrative action was "well-founded" or was a "sham," or even whether Union knowingly or recklessly made false factual representations to the State Corporation Commission. Nor could there have been any finding adverse to Union on these issues, inasmuch as it actually prevailed initially before the Commission and did so through cross-examination of respondent's witnesses concerning the need for additional wells to be drilled on respondent's property.

The willingness of courts to attach liability to the constitutional right of parties to appear in judicial and administrative proceedings unquestionably harms a party such as Union here by invading its substantial interest in freely presenting its views to the government bodies to whose jurisdiction it is subject. That is particularly the case here where Union had not initiated the proceeding but was simply exercising its right to participate in the proceeding begun by respondent. The true magnitude of the harm, however, goes far beyond this particular case or the parties involved. Putting parties such as Union to the difficult choice of either saying what they think in administrative and judicial proceedings and risking pun-

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[21] *Bill Johnson's Restaurants, Inc. v. NLRB*, 461 U.S. 731, 743 (1983).

ishment, or else keeping quiet and remaining safe, will necessarily harm the free marketplace of ideas safeguarded by the First Amendment. If parties are not free to express their positions without threat of harm, not only will the protection of the First Amendment be compromised, but the judgments of the tribunals involved will be based on inaccurate and incomplete information. Only by ensuring immunity from punishment, except where parties act for purposes other than prevailing on the merits, can the courts protect the interest of us all, litigants and the public alike, in promoting fair, accurate, and informed adjudication of matters pending before judicial and administrative tribunals.

CONCLUSION

For the foregoing reasons, the writ of certiorari should be granted to clarify the First Amendment limitations on state tort laws as applied to activities before judicial and administrative tribunals.

Respectfully submitted,

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September 30, 1985

APPENDICES

APPENDIX A

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

No. 84-1766

SARAH M. SPAETH,
Plaintiff-Appellee,

v.

UNION OIL COMPANY OF CALIFORNIA, a corporation,
Defendant-Appellant.

May 24, 1985

H.B. Watson, Jr. (Richard K. Books and Sharon L. Taylor, with him on briefs), all of Watson & McKenzie, Oklahoma City, Okl., for defendant-appellant.

Robert J. Emery, Oklahoma City, Okl. (James M. Gaitis of Emery McCandless & Gaitis, P.C. and Harry H. Selph, II and Stephen R. Stephens of Feliers, Snider, Blankenship, Bailey & Tippens, Oklahoma City, Okl., with him on briefs), for plaintiff-appellee.

Before McKAY, BREITENSTEIN and McWILLIAMS, Circuit Judges.

BREITENSTEIN, Circuit Judge.

This case is before the court for the second time. See *Spaeth v. Union Oil Company of California*, 10 Cir., 710 F.2d 1455. The only question raised on the appeal is the amount of punitive damages. On the first appeal we held

that the plaintiff-appellee, Spaeth, was entitled to recover punitive damages. Id. at 1460. This is the law of the case. *Major v. Benton*, 10 Cir., 647 F.2d 110, 112. The jury had awarded $3,000,000.00 in punitive damages and actual damages of $22,807.00. *Spaeth*, supra, 710 F.2d at 1458. We said that "the punitive award shocks our collective judicial conscience." Id. at 1460, and remanded the case saying, Id.:

> "In the exercise of our power under 28 U.S.C. § 2106, we remand the case to the district court with directions (1) to enter a judgment for the plaintiff and against the defendant in the amount of $17,542 for actual damages, (2) to set aside and vacate the award of punitive damages, (3) to order a remittitur of a substantial amount in punitive damages with due consideration to the amount needed to punish the defendant in the particular circumstances presented, and (4) if the plaintiff does not accept the remittitur, to hold a jury trial solely on the amount of punitive damages."

On remand, the trial court said, R. Vol. IX, pp. 612-613:

> "The Court has considered the record presented at trial, including the relative economic positions possessed by the plaintiff and the defendant, the fact that the plaintiff was assisted in this litigation by another, the fact that the defendant asserted as a defense that it held a 'license to drain gas,' (Opinion of the Circuit Court, p. 6), the fact that the defendant offered no explanation prior to the commencement of this action for its failure to fully develop the leasehold estate held by it, and the fact that the defendant's leasehold estate has been cancelled in part and it is now subject to an award of punitive damages. Upon consideration of these factors, and the record as a whole, this Court finds that the defendant's actions towards the plaintiff were particu-

> larly egregious and a substantial award of punitive damages is warranted so as to impress upon the defendant a responsibility to deal fairly with its royalty interest holders. Accordingly, the plaintiff is hereby directed to remit one million dollars of the punitive damages awarded by the jury within fifteen days hereof."

The record sustains the findings of the trial court.

The plaintiff remitted One Million Dollars. R. Vol. IX, p. 614. Judgment was entered for an award of Two Million Dollars as punitive damages. R. Vol. IX, p. 619.

The court found that the defendant's net worth as of September 30, 1980, as shown by its Form 10-Q filed on November 13, 1980, with the Securities and Exchange Commission was approximately three and one-third billion dollars. R. Vol. II, p. 292.

The Oklahoma statute on punitive damages, 23 O.S. § 9, provides:

> "In any action for the breach of an obligation not arising from contract, where the defendant has been guilty of oppression, fraud or malice, actual or presumed, the jury, in addition to the actual damages, may give damages for the sake of example, and by way of punishing the defendant."

The underlying purpose of the statute is to set an example and to punish the defendant for the general benefit of the public. *Garland Coal & Mining Company v. Few*, 10 Cir., 267 F.2d 785, 790; *Thiry v. Armstrong World Industries*, Okl., 661 P.2d 515, 517. Punitive damages need bear no relation to the actual damages awarded, but they must bear some relation to the injuries inflicted. *Garland, supra*, 267 F.2d at 791; *Cates v. Darland*, Okl., 537 P.2d 336, 340. The wealth of the defendant and the risk created by the defendant's conduct are substantial factors to be considered in calculat-

ing punitive damages. *Thiry, supra,* 661 P.2d at 518-519; *Smith v. United States Gypsum Co.,* Okl., 612 P.2d 251, 255. Under Oklahoma law punitive damages may be recovered in conjunction with nominal actual damages. *Beavers v. Lamplighters Realty, Inc.,* Okl. App., 556 P.2d 1328, 1333; *Moyer v. Cordell,* 204 Okl. 255, 228 P.2d 645, 650-651.

The defendant's conduct in maliciously allowing drainage of plaintiff's gas and in opposing her attempts to obtain relief, together with its net worth of three and one-third billion dollars, must be considered along with the injury inflicted, breach of an oil and gas lease implied covenant to protect against drainage. The trial court felt that the conduct of the defendant was so egregious that an award of Two Million Dollars in punitive damages was justified and necessary to punish the defendant. R. Vol. IX, pp. 612-613. We cannot say that the trial court abused its discretion.

Affirmed.

APPENDIX B

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

No. 81-1752

SARAH M. SPAETH,
Appellee,

v.

UNION OIL COMPANY OF CALIFORNIA, a corporation,
Appellant.

June 24, 1983

Robert J. Emery, Oklahoma City, Okl. (James M. Gaitis of Emery, McCandless, Gaitis, Bruehl & Gerstandt, and Harry H. Selph, II, of Fellers, Snider, Blankenship, Bailey & Tippens, Oklahoma City, Okl., with him on brief), for appellee.

H.B. Watson, Jr., Oklahoma City, Okl. (Richard K. Books of Watson, McKenzie & Moricoli, Oklahoma City, Okl., with him on briefs), for appellant.

Before McWILLIAMS, McKAY and BREITENSTEIN, Circuit Judges.

BREITENSTEIN, Circuit Judge.

This diversity action presents a claim by a lessor against a lessee for tortious breach of an Oklahoma oil and gas lease implied covenant to protect against drainage. After trial the jury found that the defendant had breached the lease and awarded both actual and punitive

damages. Subsequently, the court awarded partial lease cancellation. The appeal of the lessee raises many issues of fact and law. We affirm the jury verdict that defendant breached the lease and the court decision for partial lease cancellation. We reverse the awards of actual and punitive damages.

The basic facts are not disputed. Plaintiff-appellee Spaeth owns an undivided one-half mineral interest in approximately 160 acres of the Northeast Quarter of Section 4. In 1956 her predecessor in title made an oil and gas lease of the land to defendant-appellant Union Oil Company of California. By order of December 28, 1965, the Oklahoma Corporation Commission, hereafter Commission, designated Section 4 as a single drilling and spacing unit for the Morrow common source of supply, the oil and gas bearing formation underlying the area. Union drilled what is known as the Schneider well on Section 4. Production from the well commenced in May, 1967.

Union has the following additional interests in the immediate area: (1) approximately one-half of the working interest in Section 3 (immediately to the east of Section 4); (2) one-fourth of the working interest in Section 9 (immediately to the south of Section 4); and (3) three-eighths of the working interest in Section 10 (immediately to the southeast of Section 4).

Sections 3, 9, and 10 are also single drilling and spacing units for the Morrow common source. Each contains one well. Union operates the well on Section 3. Amoco Production Company operates the wells on Sections 9 and 10.

On February 13, 1975, Ralph Harvey, president of Marlin Oil Company, filed an application with the Commission for permission to drill an additional well on Section 4. At the time neither Harvey nor Marlin had any interest in Section 4. Union appeared before the Commission's Trial Examiner and opposed Harvey's applica-

tion. The Commission denied the application on June 11, 1975. Before filing the application, Harvey had corresponded with Union concerning the drilling of an additional well on Section 4 and Union had rejected his proposals.

Spaeth and other owners of mineral interests in Section 4, on January 29, 1976, filed an application with the Commission for authorization to drill another well on Section 4. Union appeared before the Commission and resisted the application. The Commission denied the application on June 22, 1976. Spaeth then appealed to the Oklahoma Supreme Court.

On October 25, 1976, counsel for Spaeth wrote Union that the wells in Sections 3, 9, and 10 were causing substantial drainage of gas from Section 4 which Union permitted by failing to drill another well and by opposing Spaeth's application for another well. The letter gave Union the option of drilling another well, releasing the lease within 90 days, or facing an action for lease cancellation.

The instant action was filed in state court on February 20, 1979, and removed to federal court on diversity grounds. Before the case went to trial the Oklahoma Supreme Court reversed the Commission's denial of the Spaeth application. *Spaeth v. Corporation Commission*, Okl., 597 P.2d 320. Union filed a petition for rehearing which was denied. Pursuant to the court's mandate, the Commission, on December 20, 1979, authorized another well on Section 4. Union then expressed willingness to drill an additional well if Spaeth abandoned her cancellation claim. She refused to do so. The case then proceeded to a simultaneous trial to a jury on the questions of liability and damage and to the court on the question of lease cancellation. The jury found Union liable and awarded Spaeth $22,807 in actual damages and three million dollars in punitive damages. The court ordered

lease cancellation except as to the limited right to produce and market gas and condensate from the Schneider well on Section 4. R. 296.

Plaintiff Spaeth claims fraudulent drainage by the three wells in adjoining sections. Union is the operator of one of the wells and has a substantial interest in the other two. The Spaeth well is towards the edge of the formation with less pressure than the three other wells which are located near the top of the formation. The well on the Spaeth section reaches a tighter and less productive sand than that found under the other three wells. Two witnesses for Spaeth testified as to drainage. Harvey, Tr. 170, 175-181; and Flesher, Tr. 76-80. Two witnesses for Union conceded the fact of drainage. Hughes, Tr. 278-282; and Cunningham, Tr. 431-432, 447. The fact of substantial drainage is supported by the evidence.

Oklahoma law recognizes that, absent an express provision, an oil and gas lease contains an implied covenant to protect against drainage. The prudent operator rule is usually the yardstick to determine compliance with this covenant. *Sunray Mid-Continent Oil Co. v. McDaniel*, Okl., 361 P.2d 683, 685. Union asserts that the prudent operator rule does not apply because the spacing order prevented it from drilling another well on Section 4. This argument was specifically rejected by the Oklahoma Supreme Court in *Corporation Commission v. Union Oil Company of California*, Okl., 591 P.2d 711, 715, which, after quoting 52 O.S. 1971 § 87.1(c) said:

> ". . . the statute allows the Commission to authorize the drilling of an additional well within a drilling or spacing unit upon proof that the additional well or modification of the previous order will assist in preventing waste or the protection of correlative rights of persons interested in the common source of supply."

Although Oklahoma does not appear to have determined whether, under a protection covenant, a lessee is required to seek administrative relief from a spacing and drilling order, we have held that the acceptance of an argument similar to that of Union is to give a "license to drain gas," and "[i]t would be grossly inequitable to confer such windfalls." *Cook v. El Paso Natural Gas Co.*, 10 Cir., 560 F.2d 978, 982. Union had a duty, which it could not ignore, to seek administrative relief. See *Sinclair Oil & Gas Co. v. Bishop*, Okl., 441 P.2d 436, 447.

Union opposed both Spaeth's application to the Commission for permission to drill another well on Section 4 and Spaeth's appeal from the Commission order to the Oklahoma Supreme Court. Union justifies its conduct by saying that it relied on the advice of its experts. The argument has no merit. In its decision reversing the Commission, the Oklahoma Supreme Court pointed out that before the Commission Spaeth offered evidence of an expert supported by technical data and that Union offered no expert testimony. *Spaeth v. Corporation Commission*, supra, 597 P.2d at 322. We find nothing in the record to sustain Union's claim of good faith reliance on its experts. The reasonable inferences are all to the contrary.

Union argues that the filing of this suit suspended any duties which it owed under the protection covenant. A demand for performance of an implied covenant is prerequisite to an action for breach of that covenant. *Vincent v. Tidewater Oil Programs, Inc.*, Okla., 620 P.2d 910, 916. Spaeth made her demand on October 25, 1976. That demand did not suspend any duty owed under the lease. The filing of suit to cancel or terminate a lease excuses the lessee's performance of an implied covenant. *Hoyt v. Continental Oil Co.*, Okl., 606 P.2d 560, 562. That suspension has no effect on the rights of the lessor which have accrued when suit is filed.

Before this suit was filed, gas produced from Section 4 was sold to Oklahoma Natural Gas Co. at 21.2 cents

per MCF, thousand cubic feet. After the suit was filed, Oklahoma Natural Gas agreed to pay $1.03 per MCF for gas produced from a second well on Section 4. Union says that, until the increase, the drilling of a second well was not potentially profitable and, hence, the well would not have been drilled by a prudent operator.

The evidence on profitability is conflicting. Spaeth's witness Harvey testified that a prudent operator would have drilled a well as early as 1973 and realized a profit. Tr. 174-175. Defense witness Eggebretcht calculated the return on investment would be only 3.3% on a well drilled in 1976. Tr. 347-348. Defense witness Cunningham said that a prudent operator would not have drilled in 1976 because of an unfavorable profit to investment ratio. Tr. 390. On rebuttal Harvey attacked the defense figures as omitting the value of condensate to be recovered and overestimating the costs of drilling. Tr. 474-480. He presented his analysis of the economic aspects of drilling another well in 1976 and estimated the profit to investment ratio to be five to one. Tr. 483. The jury resolved the evidentiary conflict in favor of Spaeth. Its verdict has substantial evidentiary support.

The issue of lease cancellation was submitted to, and considered by, the court as a matter of law. The court ordered cancellation of the Section 4 lease "save and except that portion of the leasehold which has been properly developed through the Schneider 1-4 well." R. 296. The court's findings of fact are consistent with the jury verdict and are not clearly erroneous. Union argues that lease cancellation, after an award of both actual and punitive damages, is an impermissible double recovery. We do not agree. The court held, R. 295, that the "actions and inactions of Union Oil Company were in breach and disregard of the duties it owed to Sarah M. Spaeth to protect her mineral estate from drainage and to fully develop that mineral estate." The court also characterized Union's conduct toward Spaeth as "either a willful,

fraudulent or grossly negligent breach of the duty owed to her." R. 296. In *Barnes v. Mack Oil Co.*, Okl., 376 P.2d 279, a trial court judgment awarding drainage damage and partial cancellation was affirmed. As to cancellation for breach of an implied covenant, the court said, *Id.* at 281, that it "must look to the facts and circumstances of each case." The trial court examined the facts and circumstances in the case at bar. We agree with it that the equities warrant partial cancellation.

Union objects to the court's instructions on various grounds, most of which relate to the application of the prudent operator rule. The instructions are consistent with the views herein stated with regard to that rule. We are not impressed with the Union argument that the instructions shifted the burden of proof. We do not read the instructions as having that effect.

The jury awarded $22,807.00 in actual damages. We find nothing in the record to sustain that award. Flesher, a witness for the plaintiff, testified that drainage until January 1, 1981, was 7.2 billion cubic feet of gas, Tr. 78; that the value of Spaeth's lost royalty on gas was $16,320.00, Tr. 81; and that her value on lost condensate royalty was $1,132.00, Id., for a total of $17,452.00. The estimates of other witnesses were even lower. See Harvey, Tr. 170, 519-520; Hughes, Tr. 280; Eggebretcht, Tr. 351-352; and Cunningham, Tr. 431-432, 447. We are not impressed with Spaeth's efforts to sustain the jury award of actual damages. Viewing the record in the light most favorable to the plaintiff, the prevailing party, the recovery of actual damages is limited to $17,452.

The jury awarded punitive damages in the amount of three million dollars. Union says that punitive damages are improper and that the award is excessive. The applicable Oklahoma statute says that in any action for breach of an obligation not arising from the contract where the defendant is guilty of fraud or oppression, actual or presumed, the jury in addition to actual damages

"may give damages for the sake of example, and by way of punishing the defendant." Okl.Stat.Ann. tit. 23, § 9 (1951).

Union argues that the case is one for breach of contract and punitive damages are not permitted under Oklahoma law. We do not agree. Plaintiff complained of both failure to drill and tortious drainage. The court instructed the jury that if it found that Union's act or omission "was maliciously, or wantonly, or oppressively done," punitive damages may be awarded. Tr. 559. The court then defined "maliciously," "wantonly," and "oppressively." Id. at 559-560. In *Misco Leasing, Inc. v. Keller*, 10 Cir., 490 F.2d 545, 549, we considered the Oklahoma law on punitive damages and said:

> ". . . when there is a reckless and wanton disregard of another's rights, malice and evil intent may be inferred and punitive damages may be awarded."

The evidence shows a reckless and wanton disregard by Union of Spaeth's rights and sustains a reasonable inference of malice and evil intent. The court properly submitted the punitive damage issue to the jury. The question is whether the award is excessive. If the award resulted from passion and prejudice, a new trial on the amount of punitive damages would be in order. Essentially the dispute was between two oil companies. The plaintiff was assisted and financed by Marlin Oil Company and it was entitled to participate in any damage award. Tr. 203-205. The trial was a contest between experts and was completely devoid of emotional overtones.

Oklahoma permits evidence of defendant's net worth to be considered in determining punitive damages. *Smith v. United States Gypsum Co.*, Okl., 612 P.2d 251, 255, and *Basden v. Mills*, Okl., 472 P.2d 889, 896. In applying Oklahoma law we have held that "exemplary [punitive] damages must bear some relation to the injuries inflicted and the cause thereof." *Garland Coal & Mining Company v. Few*, 10 Cir., 267 F.2d 785, 791.

Under the controlling Oklahoma statute, Okla.Stat.Ann. tit. 23, § 9, punitive damages may be awarded for the sake of example or by way of punishment. The deterrent or punishment value of a punitive award varies from case to case. Cf. *Cities Service Oil Co. v. Merritt*, Okl., 332 P.2d 677 with *Jones v. Lennington*, Okl.Ct.App., 629 P.2d 805. The applicable criteria are (1) the amount needed to punish, (2) in the circumstances presented. Id. at 807. The Supreme Court has characterized a punitive award as a "discretionary moral judgment." *Smith v. Wade*, —— U.S. ——, 103 S.Ct. 1625, 1638, 75 L.Ed.2d 632. Absent an award which shocks the judicial conscience, a jury's determination is inviolate. *Melcalfe v. Atchison, Topeka & Santa Fe Railway Co.*, 10 Cir., 491 F.2d 892, 898, and *Oller v. Hicks*, Okl., 441 P.2d 356, 360.

On the record presented the punitive award shocks our collective judicial conscience. When the jury returned its verdict, it did not know that the court would later cancel the lease except for the one well Union was operating. Spaeth may now lease to another oil company. The loss of lease is a circumstance for consideration in evaluating the punitive award. In denying the motion for a new trial, so far as punitive damages are concerned, the court abused its discretion by not taking into account all the circumstances pesented.

We have considered *Malandris v. Merrill Lynch, Pierce, Fenner & Smith*, 10 Cir., 703 F.2d 1152, and conclude that it is inapposite because of factual differences and because it applies Colorado law whereas the instant case is governed by Oklahoma law.

In the exercise of our power under 28 U.S.C. § 2106, we remand the case to the district court with directions (1) to enter a judgment for the plaintiff and against the defendant in the amount of $17,542 for actual damages, (2) to set aside and vacate the award of punitive dam-

ages, (3) to order a remittitur of a substantial amount in punitive damages with due consideration to the amount needed to punish the defendant in the particular circumstances presented, and (4) if the plaintiff does not accept the remittitur, to hold a jury trial solely on the amount of punitive damages.

Reversed in part and affirmed in part. The costs in this court shall be equally divided.

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF OKLAHOMA

No. CIV-79-345-T

SARAH M. SPAETH,

Plaintiff,

vs.

UNION OIL COMPANY OF CALIFORNIA,

Defendant.

[Filed May 11, 1984]

JUDGMENT ON JURY VERDICT
AND
JUDGMENT ON DECISION BY THE COURT
AND
JUDGMENT ON REMAND

On the 9th day of March, 1981, this action came on for trial pursuant to regular jury docket setting, with the jury determining the questions of liability for monetary damages and the Court reserving the equitable determination of the issue of lease cancellation, the case being simultaneously tried to a jury and to the Court on March 9, 10 and 11, 1981.

Plaintiff appeared in person and by and through her attorneys, Harry H. Selph, II, Thomas T. Rogers and Robert J. Emery and the defendant appeared through its attorneys, Richard K. Books and H. B. Watson, Jr. Both sides announced ready to proceed with the trial. A jury of six men and women and two alternates were impaneled and sworn to well and truly try the action and evidence was simultaneously presented to them and to the Court.

At the conclusion of Plaintiff's evidence the Defendant moved for a directed verdict on the grounds that Plaintiff had wholly failed to prove the essential elements of her causes of action against the Defendant. The Court heard arguments of counsel for both parties and overruled Defendant's motion.

Thereafter, the trial upon the merits continued and the Defendant presented its evidence and rested. Thereupon, Plaintiff presented rebuttal evidence. After all the evidence was presented both sides rested. Both parties then presented motions for directed verdicts which were overruled by the Court.

The jury then heard the arguments of counsel and the Court thereupon instructed the jury and at the conclusion thereof, on due deliberation, the jury upon their oaths, returned a verdict, as follows:

> We, the Jury, find in favor of the plaintiff, Sarah M. Spaeth, and against the defendant, Union Oil Company of California, and fix plaintiff's actual damages in the amt of $22,807.00.
>
> We further award the plaintiff exemplary damages in the amount of $3 Million.

3-11, 1981	/s/ Joseph Turner
(Date)	(Foreman)

The Court then polled the jury and, finding that the verdict was the verdict of each juror, received the verdict and after concluding it was in proper form directed that it be filed of record in the case.

Upon the issue of lease cancellation reserved by the Court for equitable determination, the Court, having heard the testimony of witnesses sworn and examined in open court and having reviewed the exhibits offered and received into evidence and having heard argument of

counsel and being fully advised in the premises issued its Memorandum Opinion, which was filed in this cause on March 17, 1981, setting forth its findings of fact and conclusions of law thereon and its decision that the subject oil and gas lease should be partially cancelled.

Thereafter, Defendant perfected an appeal to the United States Court of Appeals for the Tenth Circuit and on July 20, 1983, the Court entered its opinion remanding the action to the United States District Court for the Western District of Oklahoma with directions (1) to enter a judgment for the Plaintiff and against the Defendant in the amount of $17,542.00 for actual damages, (2) to set aside and vacate the award of punitive damages, (3) to order a remittitur of a substantial amount in punitive damages with due consideration to the amount needed to punish the Defendant in the particular circumstances presented, and (4) to hold a jury trial solely on the amount of punitive damages if the Plaintiff did not accept the remittitur. On April 25, 1984, this Court directed a remittitur by the Plaintiff in the amount of one million dollars. On May 8, 1984, Plaintiff filed a remittitur of one million dollars.

IT IS THEREFORE ORDERED, ADJUDGED AND DECREED:

That Plaintiff have recover from the Defendant the sum of $17,542.00 with interest thereon from March 11, 1981, at the rate of twelve per centum (12%) per annum, as provided by law, until paid and her costs of this action.

That Plaintiff have and recover from the Defendant the sum of Two Million and no/100 Dollars ($2,000,000.00) with interest thereon from March 11, 1981, at the rate of Twelve per centum (12%) per annum, as provided by law, until paid.

That the certain Oil and Gas Lease from Harry J. Galligan, as Lessor, to Union Oil Company of California,

as Lessee, dated October 29, 1956, and recorded December 8, 1956, in Book 38 Leases at page 228 of the records of the office of the County Clerk of Blaine County, Oklahoma, covering the following described tract of land in Blaine County, Oklahoma, to-wit:

> Lots 1 and 2 and the South Half of the Northeast Quarter of Section 4, Township 17 North, Range 11 West, and containing 157.69 acres, more or less,

be and the same is hereby, cancelled of record insofar and only insofar as the mineral estate of Sarah M. Spaeth is concerned, and the Defendant and all persons holding by, through or under it, are adjudged to have no right, title or interest therein and are perpetually enjoined and restrained from exercising, or attempting to exercise, any right or interest therein except the limited right to continue to produce and market gas and condensate from the Morrow Sand common source of supply as the same may be produced from, and only from, the existing bore hole or well known as the Schneider No. 1-4 well located in the Northeast Quarter of the Southwest Quarter of said Section 4; provided, that such limited right to produce and market gas and condensate shall continue only so long as such production from the Schneider No. 1-4 well shall, when considered alone, be in commercial quantities, it being intended by this Judgment that said Defendant be under the continuing duty or implied covenant under said lease for diligent and proper operation of the Schneider No. 1-4 well and for marketing the product therefrom insofar as the Morrow Sand common source of supply is concerned.

DATED this 11th day of May, 1984.

/s/ Roy G. Thompson
United States District Judge

Entered in judgment docket May 11, 1984

APPENDIX D

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF OKLAHOMA

No. CIV-79-345-T

SARAH M. SPAETH,
Plaintiff,

vs.

UNION OIL COMPANY OF CALIFORNIA,
Defendant.

[Filed Mar. 24, 1981]

JUDGMENT ON JURY VERDICT
AND
JUDGMENT ON DECISION BY THE COURT

On the 9th day of March, 1981, this action came on for trial pursuant to regular jury docket setting, with the jury determining the questions of liability for monetary damages and the Court reserving the equitable determination of the issues of lease cancellation, the case being simultaneously tried to a jury and to the Court on March 9, 10 and 11, 1981.

Plaintiff appeared in person and by and through her attorneys, Harry H. Selph, II, Thomas T. Rogers and Robert J. Emery and the defendant appeared through its attorneys, Richard E. Books and H. B. Watson, Jr. Both sides announced ready to proceed with the trial. A jury of six men and women and two alternates were im-

paneled and sworn to well and truly try the action and evidence was simultaneously presented to them and to the Court.

At the conclusion of Plaintiff's evidence the Defendant moved for a directed verdict on the grounds that Plaintiff had wholly failed to prove the essential elements of her causes of action against the Defendant. The Court heard arguments of counsel for both parties and overruled Defendant's motion.

Thereafter, the trial upon the merits continued and the Defendant presented its evidence and rested. Thereupon, Plaintiff presented rebuttal evidence. After all the evidence was presented both sides rested. Both parties then presented motions for directed verdicts which were overruled by the Court.

The jury then heard the arguments of counsel and the Court thereupon instructed the jury and at the conclusion thereof, on due deliberation, the jury upon their oaths, returned a verdict, as follows:

> We, the Jury, find in favor of the plaintiff, Sarah M. Spaeth, and against the defendant, Union Oil Company of California, and fix plaintiff's actual damages in the amount of $22,807.00.
>
> We further award the plaintiff exemplary damages in the amount of $3 Million.
>
> 3-11, 1981. /s/ Joseph Turner
>
> (Date) (Foreman)

The Court then polled the jury and, finding that the verdict was the verdict of each juror, received the verdict and after concluding it was in proper form directed that it be filed of record in the case.

Upon the issue of lease cancellation reserved by the Court for equitable determination, the Court, having

heard the testimony of witnesses sworn and examined in open court and having reviewed the exhibits offered and received into evidence and having heard argument of counsel and being fully advised in the premises issued its Memorandum Opinion, which was filed in this cause on March 17. 1981, setting forth its findings of fact and conclusions of law thereon and its decision that the subject oil and gas lease should be partially cancelled.

IT IS THEREFORE ORDERED AND ADJUDGED:

That Plaintiff have and recover from the Defendant the sum of $22,807.00 with interest thereon from March 11, 1981, at the rate of twelve per centum (12%) per annum, as provided by law, until paid and her costs of this action.

That Plaintiff have and recover from the Defendant the sum of Three Million and no/100 Dollars ($3,000,000.00) with interest thereon from March 11, 1981, at the rate of Twelve per centum (12%) per annum, as provided by law, until paid.

That the certain Oil and Gas Lease from Harry J. Galligan, as Lessor, to Union Oil Company of California, as Lessee, dated October 29, 1956, and recorded December 8, 1956, in Book 38 Leases at page 228 of the records of the office of the County Clerk of Blaine County, Oklahoma, covering the following described tract of land in Blaine County, Oklahoma, to-wit:

> Lots 1 and 2 and the South Half of the Northeast Quarter of Section 4, Township 17 North, Range 11 West, and containing 157.69 acres, more or less,

be, and the same is hereby, cancelled of record insofar and only insofar as the mineral estate of Sarah M. Spaeth is concerned, and the Defendant and all persons holding by, through or under it, are adjudged to have no right, title or interest therein and are perpetually enjoined and restrained from exercising, or attempting to

exercise, any right or interest therein except the limited right to continue to produce and market gas and condensate from the Morrow Sand common source of supply as the same may be produced from, and only from, the existing bore hole or well known as the Schneider No. 1-4 well located in the northeast Quarter of the Southwest Quarter of said Section 4; provided, that such limited right to produce and market gas and condensate shall continue only so long as such production from the Schneider No. 1-4 well shall, when considered alone, be in commercial quantities, it being intended by this Judgment that said Defendant be under the continuing duty or implied covenant under said lease for diligent and proper operation of the Schneider No. 1-4 well and for marketing the product therefrom insofar as the Morrow Sand common source of supply is concerned.

DATED this 24th day of March, 1981.

/s/ Roy G. Thompson
United States District Judge

Entered in judgment docket 3-24-81

APPENDIX E

MAY TERM—July 2, 1985

Before Honorable William J. Holloway, Jr., Honorable Jean S. Breitenstein, Honorable Robert H. McWilliams, Honorable James E. Barrett, Honorable Monroe G. McKay, Honorable James K. Logan, Honorable Stephanie K. Seymour, and Honorable John P. Moore, Circuit Judges.

No. 84-1766

SARAH M. SPAETH,
Plaintiff-Appellee.

v.

UNION OIL COMPANY OF CALIFORNIA,
a corporation,
Defendant-Appellant.

This matter comes on for consideration of appellant's petition for rehearing and suggestion for rehearing in banc in the captioned cause.

Upon consideration whereof, the petition for rehearing is denied by the panel to whom the case was argued and submitted.

The petition for rehearing having been denied by the panel to whom the case was argued and submitted, and no member of the panel nor judge in regular active service on the Court having requested that the Court be polled on rehearing in banc, Rule 35, Federal Rules of Appellate Procedure, the suggestion for rehearing in banc is denied.

/s/ Howard K. Phillips
HOWARD K. PHILLIPS
Clerk

APPENDIX F

BEFORE THE CORPORATION COMMISSION
OF THE STATE OF OKLAHOMA

Cause CD No. 43460
Order No. 122300

Applicants:	SARAH M. SPAETH, WILLIAM KELLY CRONKHITE, WINNIE MAY HOWELL and WALTER SCHNEIDER
Nature of Cause:	TO PERMIT ADDITIONAL WELL TO BE DRILLED WITHIN ESTABLISHED MORROW SPACING UNIT
Land Covered:	SECTION FOUR, TOWNSHIP SEVENTEEN NORTH, RANGE ELEVEN WEST (Sec. 4-17N-11W), BLAINE COUNTY, OKLAHOMA

REPORT OF THE COMMISSION

This Cause came on for hearing before the Corporation Commission of the State of Oklahoma on May 7, 1976, at 10:00 a.m., in the Commission Courtroom, Jim Thorpe Building, Oklahoma City, Oklahoma, on motion of the Applicant to recall said cause from the Trial Examiner's docket. The Honorable Rex Privett, Chairman; Hamp Baker, Vice-Chairman; and Jan Eric Cartwright, Commissioner; sitting.

Robert J. Emery, Attorney, appeared for the Applicants; H. B. Watson, Jr., Attorney, appeared for Union

Oil Company of California; Gordon B. Ryan, Attorney, appeared for Amoco Production Company; Harold Thweatt, Attorney, appeared for Ashland Oil, Inc.; and Nell Rhodes Fisher, Assistant Conservation Attorney, appeared for the Commission.

The Commission having heard all of the evidence and argument of counsel, took the matter under advisement and now, on this 15th day of May, 1976, the Commission being in executive session and having considered all the evidence in this cause, finds as follows:

FINDINGS

1. That this is an application of Sarah M. Spaeth, William Kelly Cronkhite, Winnie May Howell, and Walter Schneider, for an order permitting the drilling of an additional well to the Morrow formation underlying Section 4, Township 17 North, Range 11 West, Blaine County, Oklahoma, which governmental section constitutes a single drilling and spacing unit for the production of oil and gas from said formation by prior Order of the Commission.

2. That the Commission has jurisdiction over the subject matter herein; that notice has been given in all respects as required by law and by the rules of the Commission.

3. That the evidence reveals that all of the oil, gas and other mineral rights are under lease, with Union Oil Company of California owning 157.69 leasehold acres, Texaco Inc. owning 160 leasehold acres, Ashland Oil, Inc. owning 160 leasehold acres, and Getty Oil Company owning 156.8 leasehold acres. The Applicants have no oil and gas leasehold ownership and do not have the right to drill a well within the unit.

4. That the evidence further reveals that Ralph L. Harvey owns an interest in the oil, gas and other minerals in and under the Southeast Quarter and the North-

west Quarter of said Section 4 by virtue of mineral conveyances from Winnie M. Howell and the Board of National Missions of the United Presbyterian Church in the United States of America. That said conveyances provide that the grantors in each of said conveyances reserve all of the existing 1/8 lessor's royalty attributable to the interest conveyed in and to, but only in and to, the existing well located on said unit. Said interest is subject to valid and subsisting oil and gas leases.

5. This Commission, by Order No. 61106, designated said Section 4 as a single drilling and spacing unit for the production of oil and gas from the Morrow common source of supply. Thereafter, Union Oil Company of California, as operator of said unit, drilled its #1 Schneider Well, which well has been producing oil and gas in commercial quantities since April, 1967. That said Order No. 61106 provided for the drilling of only one well on said drilling and spacing unit.

6. That the evidence introduced did not establish a substantial change of conditions or a substantial change of knowledge of condition since Order No. 61106 was entered. The evidence establishes that each of the peripheral eight sections surrounding said Section 4 contain a single producing Morrow well, all of which are located on the pattern established by orders of this Commission. The evidence fails to establish the violation of the correlative rights of the applicants or of the owners of the oil and gas rights in and under the unit in question, as well as the eight peripheral units.

7. Therefore, taking into consideration all of the evidence presented and the arguments of counsel, the Commission finds that in the interest of securing the greatest ultimate recovery of petroleum hydrocarbons from the reservior, the prevention of waste and the protection of correlative rights, this application should be denied.

ORDER

IT IS THEREFORE ORDERED by the Corporation Commission of Oklahoma as follows:

THAT the Application of Sarah M. Spaeth, William Kelly Cronkhite, Winnie May Howell, and Walter Schneider for an order permitting the drilling of an additional well to the Morrow common source of supply underlying Section 4, Township 17 North, Range 11 West, Blaine County, Oklahoma, be and the same is hereby denied.

DONE AND PERFORMED this 22nd day of June, 1976.

CORPORATION COMMISSION
OF OKLAHOMA

/s/ [Illegible]
Chairman

/s/ [Illegible]
Vice-Chairman

/s/ [Illegible]
Commissioner

APPENDIX G

IN THE SUPREME COURT
OF THE STATE OF OKLAHOMA

No. 49,954

SARAH M. SPAETH, WILLIAM KELLY CRONKHITE,
WINNIE MAY HOWELL and WALTER SCHNEIDER,
Appellants,

vs.

CORPORATION COMMISSION OF THE STATE OF OKLAHOMA,
UNION OIL COMPANY OF CALIFORNIA,
ASHLAND OIL, INC. and GETTY OIL COMPANY,
Appellees.

[Filed May 8, 1979]

Appeal from the Corporation Commission
of the State of Oklahoma

Appellants sought an order which would have permitted the drilling of an additional well on a drilling and spacing unit established by the Corporation Commission. Appellants were denied relief and they appealed.

ORDER REVERSED

Robert J. Emery Lytle Soulé & Emery Oklahoma City, Oklahoma	For Appellants,
H. B. Watson, Jr., Watson, McKenzie & Moricoli Oklahoma City, Oklahoma	For Appellee Union Oil Company of California
C. Harold Thweatt Crowe, Dunlevy, Thweatt, Swinford, Johnson & Burdick Oklahoma City, Oklahoma	For Appellees Ashland Oil, Inc. and Getty Oil Company.

IRWIN, V.C.J.

Appellants, Sarah M. Spaeth and various other mineral owners, filed an application with the Corporation Commission for a modification of a previous order creating 640 acre drilling and spacing units within the common source of supply to permit the drilling of an additional well to protect appellants from drainage and consequent prejudice of their correlative rights.[1] Union Oil Company, the well operator in the affected drilling and spacing unit, Ashland Oil Company, Inc., and Getty Oil Company, adjoining operators, intervened as contestants to the application. By Order No. 122,300, Commission denied appellants' requested modification, and they appealed.

Union first contends that appellants had no standing to request the modification. 52 O.S. 1971, § 87.1(a) authorizes the Commission to enter an order after hearing upon petition of any person owning an interest in minerals embraced within the common source of supply or the right to drill upon lands embraced within the common source of supply. *Texas Oil and Gas Corporation v. Rein*, Okl., 534 P.2d 1277 (1975). Also, 52 O.S. 1971, § 112, provides in part:

> "Any person affected by any Legislative or administrative order of the Commission shall have the right at any time to apply to the Commission to repeal, amend, modify or supplement the same * * *."

Appellants not only owned an interest in the minerals involved but had been affected by the Commission's order establishing the drilling unit in the common source of supply. We hold appellants had standing to seek the relief requested. Whether they are entitled to any relief is an entirely different matter.

---

[1] Appellants sought authority to drill an additional well on the drilling and spacing unit and did not seek two allowables, but only a single allowable.

The record discloses a common source of supply for natural gas in the Morrow formation, underlying part of Township 17, Range 11 West, Blaine County, Oklahoma. By Order No. 59,245, entered June 17, 1965, the Commission created 640 acre drilling and spacing units for the Morrow underlying Sections 10 through 15 and 22 through 24 of Township 17. This order was entered on the strength of information obtained from a producing well drilling in Section 14. By Order No. 61,106, entered December 28, 1965, the Commission extended Order No. 59,245 to include Sections 1 through 5, 8, 9, 16, 17, 20, 21, and 25 through 29 of Township 17. Evidently, Order No. 61,106 was entered on the strength of information obtained from the well in Section 14 as there was no additional development in the area between the June and December order.

In 1966 and 1967 wells were drilled and completed in Sections 3, 4, 9 and 10. Appellants are mineral owners of acreages underlying Section 4. The well in Section 4 is, relatively speaking, a poor well. Testimony on behalf of appellants was that past production and potential future recovery from adjoining wells east, southeast and south of Section 4 was and would continue to be many times greater than in Section 4. Appellants' expert believed that porosity factors are such in the common source of supply that these better producing wells have been and will continue to drain gas from under Section 4. That testimony was based on data resulting from the four wells drilled since the last order.

The Commission, in denying appellants' application for modification, made the following findings:

> "6. That the evidence introduced did not establish a substantial change of conditions or a substantial change of knowledge of conditions since Order No. 61,106 was entered. * * * The evidence fails to establish the violation of the correlative rights of the

applicants or of the owners of the oil and gas rights in and under the unit in question * * *."

A spacing order which has become final may be modified only upon substantial evidence which shows a change in conditions, or a change in knowledge of conditions, arising since the last order. *Phillips Petroleum Co. v. Corporation Commission*, Okl., 461 P.2d 597 (1969). As in other Commission proceedings, the substantial evidence rule controls in appeals involving oil and gas conservation orders. *French v. Champlin Exploration, Inc.*, Okl., 534 P.2d 1302 (1975). This Court had on numerous occassions repeated the definition of "substantial evidence". See *Central Oklahoma Freight Lines v. Corporation Commission*, Okl., 484 P.2d 877 (1971).

Virtually all of the evidence before the Commission was presented by appellants. Based upon data obtained as a result of the wells in Section 3, 4, 9 and 10, their expert testified that the wells in Section 3, 9 and 10 were draining Section 4. He said that we now have information involving the reservoir that we did not have when the first orders were entered; and that the changes in knowledge and conditions are substantial changes. This expert was of the opinion that the well in Section 4 was not capable of protecting Section 4 from drainage from the wells in Section 3, 9 and 10. In order to stop the drainage, he was of the opinion an additional well had to be drilled in Section 4. The expert's opinion was supported by technical data. Appellees offered no expert testimony but did cross-examine appellants' witness on all matters. Notwithstanding this lengthy questioning, appellants' expert testimony remained consistent. We can only conclude there is no substantial evidence that will support Commission's finding that the "evidence introduced did not establish a substantial change of conditions or a substantial change of knowledge of conditions" since the previous spacing order, and its finding that "the evidence fails to establish the violation of the correlative

rights of the applicants or of the owner of the oil and gas rights in and under the unit in question." Appellants are entitled to a reversal of the Commission's order.

Appellants suggest that under 52 O.S. 1971, § 112, this Court on appeal, "may itself make the order which the Commission should have made". Section 112 was enacted in 1933 and at that time the Supreme Court had "jurisdiction to review, reverse, correct or annul any action of the Commission within the scope of its authority * * *." See Oklahoma Constitution, 1931, § 13605. Section 13605 was amended in 1941, and Article 9, § 20 of the Oklahoma Constitution now provides that the Supreme Court "shall enter judgment, either affirming or reversing the order of the Commission appealed from."

Order reversed.

LAVENDER, C.J., WILLIAMS, HODGES, BARNES, SIMMS, HARGRAVE, OPALA, JJ., CONCUR. DOOLIN, J., DISSENTS.